Nos. 20877 and 20877A

IN THE UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

GRANT E. NEAGLE and NORMA C. NAEGLE,

Petitioners

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent

ON PETITIONS FOR REVIEW OF THE DECISIONS OF THE TAX COURT OF THE UNITED STATES

BRIEF FOR THE RESPONDENT

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OPINION BELOW

The memorandum findings of fact and opinion of the Tax Court (I-R. 54-62) are not officially reported.

JURISDICTION

The petitions for review (I-R. 88-103) in this case involve deficiencies in income tax in the total amount of $16,718.57 against Grant E. Naegle for the years 1956 and 1960 and in the total amount of $249.11 against his wife, Norma, for the years 1959 and 1960. On March 18, 1963, the Commissioner of Internal Revenue mailed notices of the above deficiencies to the taxpayers. (I-R. 11-17, 31-35.) Taxpayers filed timely petitions with the Tax Court for a redetermination of those deficiencies under Section 6213 of the Internal Revenue Code of 1954. (I-R. 1-17, 27-35.) The decisions of the Tax Court were

entered on November 10, 1965 (I-R. 80-81, 86-87). Taxpayers petitioned for review by this Court on February 9, 1960 (I-R. 88-103), within the three-month period prescribed by Section 7483 of the Internal Revenue Code of 1954. Jurisdiction is conferred on this Court by Section 7482 of that Code.

QUESTIONS PRESENTED

1. Whether the Tax Court correctly held that funds embezzled in 1956 were includible in taxpayer's[1] income in that year.

2. Whether the Tax Court's finding that taxpayer failed to prove that he had net operating losses in prior years to carry over and apply to income in the year 1956 is clearly erroneous.

3. Whether the Tax Court correctly upheld the Commissioner's disallowance of deductions in 1960 for charitable contributions and repayment of embezzled funds where taxpayer presented no evidence to substantiate the claimed deductions.

4. Whether the Tax Court's finding that taxpayer and his wife each contributed over half the support of one of their two children (allowing each of them to deduct one dependency exemption) is clearly erroneous.

STATUTES AND REGULATIONS INVOLVED

The statutes and Regulations involved are set out in the Appendix, *infra*.

1/ The principal issues involved in the case concern only the activities of Grant Naegle, referred to for convenience as "taxpayer". Taxpayer Norma Naegle will be referred to as "taxpayer's wife".

STATEMENT

The facts, some of which were stipulated, were found by the Tax Court (I.R. 54-62), as follows:

Grant and Norma Naegle are husband and wife living in Phoenix, Arizona, with their two daughters. All of their returns were filed with the District Director of Internal Revenue in Phoenix. Taxpayers filed timely joint income tax returns for each of the years 1957, 1958 and 1961. Norma filed timely separate income tax returns for each of the years 1959 and 1960 and Grant filed a separate delinquent income tax return for the year 1960. Prior to April 16, 1957, Grant mailed to the District Director's office a printed 1956 Form 1040 on which he wrote that he had earned nothing in 1956, had been placed in receivership, and had been supported by his wife's separate income for that year. (I-R. 55-56.)

Grant operated a property management and real estate brokerage business in Phoenix, Arizona, under the trade name of Naegle Property Services, from 1951 until August 6, 1956. On October 21, 1958, taxpayer was convicted, upon his plea of guilty, in the Superior Court of Maricopa County, Arizona, of the charge of grand theft by embezzlement. He was given a ten-year suspended sentence conditional upon his repaying the funds to a court-appointed trustee. Pursuant to this judgment, a trust agreement was drawn up on May 8, 1959, under which the trustee was a twenty-page list of 274 unsecured creditors and the amounts of the claims totaling $71,088.32, and one page showing two claims called "Priority Claims Allowed" totaling $4,120.82. (I-R. 58.)

The Commissioner of Internal Revenue determined that Grant had income of $35,715.90 in 1956, of which $35,000 represented income from the money that he embezzled.[2/] The remaining $715.90 was Grant's share in the community income earned by his wife. (I-R. 58.)

On Norma's separate income tax return for 1959, she reported wages received in the sum of $3,683.52. On Grant's separate income tax return for that year he reported wages in the sum of $12,226.98. The Commissioner determined that the total wage income of both, or $15,910.50, was community income, with one-half, or $7,955.25, taxable on each separate return for that year. This resulted in a determination of overassessment against Grant for the year 1959, and a deficiency in the same amount against Norma for that year. (I-R. 58-59.)

In his 1960 income tax return, Grant reported $7,944.64 as wages received and deducted $5,000 paid as partial restitution of the money embezzled in 1956. He also deducted $300 in charitable contributions to a named (but unreadable) "missionary fund, red cross, and other contributions". The Commissioner disallowed both of the above deductions and determined that one-half of the total of Grant's and Norma's wages was his share of their community income. This gave Grant an overstatement in taxable wages of $1,818.57 on his return and created an understatement of that amount on Norma's return. (I-R. 58.) The Commissioner also determined that the two children were supported equally by Grant and Norma. Since Norma had taken exemptions for both daughters on all of her returns,

2/ The total amount embezzled was $75,000 which was set off against a $40,000 net operating loss incurred in the business in that year. (I-R. 47-48, 58.)

he disallowed one exemption on each of Norma's returns but added one to each of Grant's returns. (I-R. 59.)

In the Tax Court, taxpayers claimed that they had entered into an oral agreement that the income of each would remain separate income of that spouse. Grant contended that his business had sustained net operating losses in the years prior to 1956, which should be carried over and set off against his gains from embezzlement in that year. There was no evidence introduced on the issues of deductions taken by Grant on his 1960 return or on the Commissioner's adjustments to exemptions for dependents in the years 1959 and 1960. (I-R. 60-62.)

The Tax Court found that Grant and Norma had made a valid oral agreement under Arizona law to maintain separate property and that the Commissioner erred in treating their earnings as community property. The Commissioner does not seek review of this determination. The Tax Court upheld the Commissioner's finding that Grant had received $35,000 of income in the year 1956, and held that taxpayer failed to prove the existence of net operating losses from prior years to be offset against this income. The Tax Court also upheld the Commissioner's disallowance of Grant's claimed deductions in 1960, and the allocation of the exemptions between taxpayers in 1959 and 1960. (I-R. 60-62.) Taxpayers filed motions for rehearing which were denied. (I-R. 63-75.) Decisions were entered on November 10, 1965. (I-R. 80-81, 86-87.) From that action, taxpayers have filed and prosecuted the instant petitions for review.

SUMMARY OF ARGUMENT

The Tax Court correctly held that funds embezzled in 1956 were income to taxpayer in that year. The Supreme Court's holding in 1961 (James v. United States, 327 U.S. 404) that money secured through embezzlement must be included in income applies to the years prior to 1961 for the purpose of determining civil tax liability. All of the courts which have passed upon this issue have been unanimous in so holding.

The exact amount includible in income for the year 1956 was computed on the basis of stipulated facts. Taxpayer's principal theory in the Tax Court and in this Court is that he sustained net operating losses in the years 1951 through 1955 which he is entitled to carry over and apply against income received in 1956. It is axiomatic that in order to prevail on this theory, taxpayer must prove the amount of the losses claimed. The evidence adduced at the hearing, rather than showing the extent of the net operating losses, proved only that such losses, if any, were impossible to determine. The Tax Court's finding that taxpayer had no net operating loss carry over to the year 1956 reflects the evidence and is not clearly erroneous.

Taxpayer claimed deductions in the year 1960 for charitable contributions and repayment of funds embezzled in 1956. He offered no evidence to substantiate such deductions, and the Tax Court correctly concluded that he had abandoned the claims. Nothing in his brief in this court would contradict that conclusion.

Taxpayer and his wife had separate income and filed separate returns for the years 1959 and 1960. Taxpayer's wife deducted both dependency exemptions allowable for their two minor children on her returns for those years. The Commissioner determined that she was entitled to deduct only one exemption and that taxpayer must take the deduction for the other exemption on his return. Taxpayer's wife failed to prove in the Tax Court that she had contributed over one-half of the support of both children from her separate income or property under these circumstances, the Tax Court properly upheld the Commissioner's determination that each must take one dependency exemption on his or her separate returns for the years involved.

ARGUMENT

I

THE TAX COURT CORRECTLY HELD THAT TAXPAYER RECEIVED $35,000 IN TAXABLE INCOME FROM EMBEZZLED FUNDS IN THE YEAR 1956

Taxpayer was convicted on his plea of guilty of embezzling funds in the year 1956. His sentence was suspended on condition that he make restitution of the sum wrongfully embezzled in the approximate amount of $75,000. No part of the embezzled funds was reported on his federal income tax return for that year. The Commissioner allowed taxpayer a deduction of $40,000 for business losses incurred in that year and determined that he had under-reported his taxable income in the net amount of $35,000. (I-R. 56, 58.) Taxpayer contends, in the Tax Court and in this Court, that funds embezzled prior to the Supreme Court's

decision in James v. United States, 366 U.S. 213, in 1961 are not includible in income (I-R. 94-95) and that, if they are, the Commissioner' determination of the amount includible in taxable income is arbitrary and capricious (Br. 8, 13-17),3/ and that, moreover, he is entitled to apply net operating losses incurred in prior years against income realized in the taxable year 1956 (Br. 8, 36-48). The Commissioner contends that there is substantial evidence in the record to support the finding that embezzled funds in the amount of $35,000 were properly included in net taxable income in the year 1956 and that there is no evidence of record to substantiate taxpayer's claimed net operating loss carry-overs from prior years. Accordingly, the Tax Court's finding that taxpayer understated his income by $35,000 for the year 1956 is not clearly erroneous and should be affirmed under established standards of review. Commissioner v. Duberstein, 363 U.S. 278; United States v. Gypsum Co., 333 U.S. 364; Burke v. Commissioner, 283 F. 2d 487 (C.A. 9th); Clark v. Commissioner, 266 F. 2d 698 (C.A. 9th).

A. Embezzled funds are taxable income to the embezzler.

The Supreme Court held in 1961 that embezzled money constitutes taxable income to the embezzler (James v. United States, 366 U.S. 213),

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3/ Taxpayer Grant Naegle's brief (pp. 50-51) contains the material portions of taxpayer Norma Naegle's argument. For convenience, all "Br." references will be to taxpayer Grant Naegle's brief.

overruling its decision entered in 1946 in Commissioner v. Wilcox, 327 U.S. 404. See also Rutkin v. United States, 343 U.S. 130. Taxpayer urges that James overruled Wilcox only prospectively and that funds embezzled prior to the James decision should, therefore, be excluded from gross income. The Tax Court correctly held, however, that funds taxpayer embezzled in 1956 were includible in gross income for the purpose of computing his income tax liability for that year.

It is true, as this Court had held, that a defendant who embezzled funds in the years before the James decision could not be guilty of a willful criminal evasion of tax since the earlier Wilcox decision--that embezzled funds need not be reported as income--negated the requisite element of criminal intent. Beck v. United States, 298 F. 2d 622 (C.A. 9th), certiorari denied, 370 U.S. 919. Willfulness, however, is not an element in civil tax liability. Indeed, the problem of criminal responsibility for evasion in James would not have occured had the decision not been specifically premised on the understanding that the reversal of Wilcox was to have retrospective effect with regard to the inclusion of funds in gross income. Otherwise, the defendant in James that embezzled funds are income within the meaning of the Internal Revenue Code was therefore applicable to determine taxpayer's civil tax liability for the year 1956. The cases following James have been unanimous in holding that the decision applied to funds embezzled prior to 1961. United States v. Siano, 356 F. 2d 927 (C.A. 2d); Geiger's Estate v. United States, 352 F. 2d 221 (C.A. 8th), certiorari denied, 382 U.S. 1012; Adame's Estate v. Commissioner, 320 F. 2d 811, 814 (C.A. 5th)

(as to the year 1953, which was not barred by the statute of limitations); Stoller v. United States, 320 F. 2d 340, 344 (Ct. Cl.); Nerem v. Commissio 41 T.C. 338, 344; Muldrow v. Commissioner, 38 T.C. 907, 912; see Leaf v. Commissioner, 295 F. 2d 503 (C.A. 6th). Dicta to the same effect are present in Sowell v. Commissioner, 302 F. 2d 177, 181 (C.A. 5th); Donohue v. Commissioner, 323 F. 2d 651, 652 (C.A. 7th), certiorari denied, 376 U.S. 911; United States v. Goldberg, 330 F. 2d 30, 39 (C.A. 3d), certiorari denied, 377 U.S. 953. All of the above cases except United Sta v. Goldberg are civil tax cases.

Taxpayer argues (Br. 8, 13-15) that the Commissioner's determination that $35,000 of the embezzled funds should be included in adjusted gross income was arbitrary and capricious. The $35,000 figure, however, is based on the following stipulated facts in the record:

Taxpayer was convicted on October 21, 1958, upon his plea of guilty, of grand theft by embezzlement. (I-R. 44-45.) The judgment in that case (Stip. Ex. 10-J) clearly stated that taxpayer had wrongfully embezzled the approximate sum of $75,000.4/ Taxpayer had gross income from his business of at least $33,890.32 in 1956 (I-R. 47) and incurred expenses of $71,119.92 (I-R. 48), thus sustaining a loss of $40,0

4/ The relevant portion of the judgment is reproduced in the Tax Court's opinion at (I-R. 56A.)

5/ The $40,000 figure is generous to the taxpayer since, as stipulated (I-R. 47-48) the $33,890.32 does not include all of taxpayer's business receipts, but only those deposited in his bank account.

The $35,000 of unreported income represents the net amount of embezzled funds after the deduction of taxpayer's business losses.

The Commissioner's determination that the total amount of embezzled income was realized in the year 1956 is not disputed by taxpayer, nor is it in any way contradicted by the facts adduced at the hearing. Consequently, the Tax Court correctly held that taxpayer realized income in the amount of $35,000 which he failed to report in the year 1956.

B. Taxpayer is not entitled to an offset against income in 1956 based upon alleged net operating losses carried forward from prior years

Taxpayer's principal theory in the Tax Court (II-R. 5) and on through review (Br. 21, 35-36, 41-47) is that he was entitled to apply alleged net operating losses in prior years against any gain realized in 1956 under Section 172(a) of the Internal Revenue Code of 1954 Appendix, infra.[6/] In order to prevail on this theory, taxpayer must prove the amount of the losses claimed, and that they were not absorbed by application to income in other years by carry-backs and carry-over. Johnson v. United States, 291 F. 2d 908 (C.A. 9th); Allied Central Stores, Inc. v. Commissioner, 339 F. 2d 503 (C.A. 2d), certiorari denied, 381 U.S. 903; Marshall v. Commissioner, 240 F. 2d 185 (C.A. 5th).

6/ Some of the years (1951-1954) for which taxpayer claims net operating losses come under Section 122(b) of the Internal Revenue Code of 1939 (26 U.S.C. 1952 ed., Sec. 122) (added to the 1939 Code by Section 211(b), Revenue Act of 1939, c. 247, 53 Stat. 862, and amended by Section 215(a), Revenue Act of 1950, c. 994, 64 Stat. 906) and the (footnote continued on following page)

As the Fifth Circuit said in Marshall v. Commissioner, supra, at p. 188--

> It was incumbent upon petitioners to introduce convincing evidence upon which the Tax Court could fairly and accurately determine any additional allowable deductions. This they failed to do.

The evidence adduced by taxpayer at the hearing, rather than proving the extent of net operating losses, showed only that such losses, if any, were impossible to determined. 7/ Taxpayer himself admits that he could never compute the extent of his losses in the taxable years 1954 and 1955. (II-R. 51.) Nelson Tompkins, who took

6/ (footnote continued from preceding page)

transitional provisions of Section 172(g) of the Internal Revenue Code of 1954. Since we argue that taxpayer has failed to prove that he is entitled to any loss carry-over from prior years, the technical variations in treatment of the years in question are not material. See, e.g. Pacific Rock & Gravel Co. v. United States, 297 F. 2d 122 (C.A. 9th); S. Rep. No. 1622, 83d Cong., 2d Sess., p. 932 (3 U.S.C. Cong. & Adm. News (1954) 4621, 4662).

7/ Taxpayer offers evidence on appeal that his counsel never submitte at the Tax Court hearing. This evidence cannot now be presented under Rule 31 of this Court's Rules of Practice. His motions for a new trial to permit the introduction of additional new evidence (I-R. 64-75) were addressed to the sound discretion of the Tax Court. Bankers Coal Co. v. Burnet, 287 U.S. 308; Minneci v. Commissioner, 368 F. 2d 161 (C.A. 7th); Henry v. Commissioner, 362 F. 2d 640 (C.A. Goodman v. Commissioner, 200 F. 2d 681 (C.A. 2d); Arc Realty Co. v. Commissioner, 295 F. 2d 98, 107 (C.A. 8th); Francis Edward McGillick Foundation v. Commissioner, 278 F. 2d 643, 649 (C.A. 3d). There is no showing that the Tax Court abused its discretion in refusing to grant taxpayer's motion, or that the evidence tendered was not available to his counsel at the time of hearing. See Greenspahn v. Joseph E. Seag & Sons, Inc., 186 F. 2d 616 (C.A. 2d).

over the business for four or five months in 1956, actually made a profit of $20,000 in that time. (II-R. 39-41.) He testified that in the years he knew taxpayer (1951-1956), the latter did a "terrific rental business." (II-R. 37.) Mr. Tompkins also stated that taxpayer's "records if you can call them that were chaotic, misplaced and unreliable." (II-R. 43)[8/] The only other witness on taxpayer's behalf was his sister, Betty Bland, who worked for him from August, 1954, to July, 1956. (II-R. 18-19.) Her testimony was inconclusive at best, and often contradictory. She estimated the loss in 1954 to be $30,000, based on the amount of payments made to the operating fund (from which expenses were paid) from the escrow fund (monies collected on behalf of landlords and payable to them). (II-R. 27.) Yet, for the year 1955, she stated that "accurate information couldn't be stated because the checks that were drawn on the operating account weren't a true picture of it." (II-R. 29.) Although she claimed to personally record everything that came into the office (II-R. 33), there were ten or fifteen people working on the books (II-R. 32). The testimony adduced at trial, on which taxpayer placed such heavy reliance in his brief, only supports the Tax Court's finding that "The evidence fails completely to show that there were any net operating loss carryovers available to reduce the 1956 income." (I-R. 61.)

8/ The taxpayer contends that the trial court erred in admitting only the portion of a letter written by Tompkins which pertained to the question he was being asked on cross-examination, and excluding the rest. (Br. 9, 51-52). The court properly exercised its judicial discretion in limiting the record to such matters as were here relevant, and taxpayer fails to show either abuse of that discretion or that the exclusion was prejudicial.

It is clearly within the province of the trier of fact to evaluate the testimony of witnesses in the light of their demeanor and credibility. Commissioner v. Duberstein, supra; United States v. Gypsum Co., supra; Clark v. Commissioner, supra. See Rule 52(a) of the Federal Rules of Civil Procedure. Taxpayer's failure to introduce convincing evidence upon which the Tax Court could fairly and accurately determine any net loss carry-overs was fatal to his claims, and the Tax Court correctly held that he was not entitled to carryover any of his asserted net operating losses for prior years to the year 1956.

II

THE TAX COURT CORRECTLY HELD THAT TAXPAYER FAILED TO SUBSTANTIATE HIS CLAIM TO DEDUCTIONS IN THE YEAR 1960 FOR ALLEGED CHARITABLE CONTRIBUTIONS UNDER SECTION 170(a)(1) OF THE INTERNAL REVENUE CODE OF 1954 AND FOR REPAYMENT OF FUNDS EMBEZZLED IN 1956

Taxpayer claims deductions for the year 1960 for $5,000 as repayment of funds under the trust agreement entered into in 1956 and for $300 in alleged charitable contributions.[9] (I-R. 58.) Taxpayer offered no evidence to substantiate the deductions in the

9/ Money received by taxpayer under claim of right must be included in income in the year received even though taxpayer is required in a later year to repay the sum. North American Oil v. Burnet, 286 U.S. 417; United States v. Lewis, 340 U.S. 590. Under the claim of right doctrine (which applies to embezzled funds under James v. United States supra,) taxpayer can deduct repayments in the year in which they are made. Section 1341 of the Internal Revenue Code of 1954 (26 U.S.C. 1964 ed., Sec. 1341) (amended by Section 60, Technical Amendments Act of 1958, P.L. 85-866, 72 Stat. 1606) provides for tax treatment of the deduction in the year of repayment. It is axiomatic, however, that taxpayer must first prove actual repayment before the question of tax consequences of such repayment is reached.

Tax Court and his only argument on appeal seems to be a semantic quibble, i.e., whether the payment was for embezzled funds or "payment on restitution under sentence of embezzlement, due to operating losses." (Br. 49.) Regardless of what it is called, it seems incredible that taxpayer has no record at all to substantiate the payment of such a large sum of money. The Tax Court's conclusion (I-R. 62) that he had abandoned the claim, in absence of any evidence whatsoever on the issue, was certainly justified. Commissioner v. Duberstein, supra.

Section 170(a)(1) of the Internal Revenue Code of 1954, Appendix, infra, provides that there shall be allowed as a deduction any charitable contribution (defined in subsection (c)) payment of which is made within the taxable year. It further provides that a charitable contribution shall be allowed as a deduction only if verified under regulations prescribed by the Secretary or his delegate. A taxpayer claiming a charitable deduction, just as in the case of any other claimed deduction, must be prepared to substantiate the amount of his payments. Bradford v. Commissioner (C. A. 2d), decided April 1, 1965 (15 A.F.T.R. 2d 1106), certiorari denied, 382 U.S. 868; Birnbaum v. Commissioner, 117 F. 2d 395 (C. A. 7th); Panek v. Commissioner; 24 T.C.M. 650, affirmed per curiam September 26, 1966 (C. A. 7th) (18 A.F.T.R. 5981). See Section 1.170-1(a), Treasury Regulations on Income Tax (1954 Code), Appendix, infra. Once again, taxpayer submitted no evidence directed to the substantiation of any of the charitable contributions claimed, or to prove that the contributions were made to organizations which qualify under Section 170(c). See Riker v. Commissioner, 224 F. 2d 220 (C. A. 9th), certiorari denied, 355 U.S. 839. The Tax Court

was justified in concluding that taxpayer had abandoned this issue also. Nothing in his brief in this Court would contradict that conclusion.

III

THE TAXPAYER'S WIFE WAS PROPERLY DENIED DEPENDENCY DEDUCTIONS FOR BOTH CHILDREN WHERE SHE FAILED TO PROVE A CONTRIBUTION OF MORE THAN ONE-HALF OF EACH CHILD'S TOTAL SUPPORT

Taxpayer and his wife, Norma, filed separate returns and maintained separate property for the years 1959 and 1960. They had two minor children. Taxpayer's wife, took both of the dependency deductions allowed by Section 151 of the Internal Revenue Code of 1954, Appendix, infra, on her returns for those years. The Commissione determined that she was entitled to deduct only one child on his return. The Tax Court upheld the Commissioner's determination because taxpayers failed to show that it was incorrect. (I-R. 62.)

Section 152 of the Internal Revenue Code of 1954, Appendix, infra, permits a taxpayer a dependency deduction for an individual, provided that certain relationship, support, and citizenship or residency tests are met. The burden is on the taxpayer to prove the factors prerequisite to the establishment of the claimed dependency deductions, including the factor of contributions to the support of the individual. Trowbridge v. Commissioner, 268 F. 2d 208 (C.A. 9th); Rezazadeh v. Commissioner, 356 F. 2d 898 (C.A. 7th); Mawhinney v. Commissioner, 355 F. 2d 462 (C.A. 3d).[10/]

10/ Taxpayers' reliance on Goold v. Commissioner, decided January 6, 1949 (8 T.C.M. 2), affirmed, 182 F. 2d 573 (C.A. 9th) (Br. 51), is misplaced. There the court did not disturb the husband and wife's allocation of exemptions because the wife was not a party to the case.

In order to meet the support test, taxpayer's wife must prove that she contributed over half of the "entire amount of support which the individual received." Treasury Regulations on Income Tax (1954 Code), Sec. 1.152-1(a)(2)(i), Appendix, infra. In the instant case, there was no evidence that both children received over half of their support from their mother, apart from her statements that "we lived off of my income." (II-R. 66.) Taxpayer's wife reported income of \$3,683.52 and \$4,307.50 in the years 1959 and 1960, respectively. He reported income in the amount of \$12,226.98 and \$7,944.64, respectively, in the same years. (I-R. 58-59.) The Commissioner reasonably determined that they each contributed one-half of the support of one child from their separate incomes, and that each was, therefore, entitled to deduct one dependency exemption. Evidence to the contrary was essential to the claim of taxpayer's wife, and the Tax Court decision should be affirmed on that basis. Rezazadeh v. Commissioner, supra.

CONCLUSION

For the reasons stated, the decisions of the Tax Court are correct and should be affirmed.

Respectfully submitted,

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JANUARY, 1967.

CERTIFICATE

I certify that, in connection with the preparation of this brief, I have examined Rules 18, 19 and 39 of the United States Court of Appeals for the Ninth Circuit, and that, in my opinion, the foregoing brief is in full compliance with those rules.

Dated: ____________________day of January, 1967.

____
Attorney

APPENDIX

Internal Revenue Code of 1954:

SEC. 151. ALLOWANCE OF DEDUCTIONS FOR PERSONAL EXEMPTIONS.

(a) Allowance of Deductions.--In the case of an individual, the exemptions provided by this section shall be allowed as deductions in computing taxable income.

* * *

(e) Additional Exemption for dependents.--

(1) In general.--An exemption of $600 for each dependent (as defined in section 152)--

(A) whose gross income for the calendar year in which the taxable year of the taxpayer begins is less than $600,

* * *

(3) Child defined.--For purposes of paragraph (1) (B), the term "child" means an individual who (within the meaning of section 152) is a son, stepson, daughter, or stepdaughter of the taxpayer.

* * *

(26 U.S.C. 1964 ed., Sec. 151.)

SEC. 152. DEPENDENT DEFINED.

(a) General Definition.--For purposes of this subtitle, the term "dependent" means any of the following individuals over half of whose support, for the calendar year in which the taxable year of the taxpayer begins, was received from the taxpayer (or is treated under subsection (c) as received from the taxpayer):

(1) A son or daughter of the taxpayer, or a descendant of either,

* * *

(26 U.S.C. 1964 ed., Sec. 152.)

SEC. 170. CHARITABLE, ETC., CONTRIBUTIONS AND GIFTS.

(a) Allowance of Deduction.--

(1) General rule.--There shall be allowed as a deduction any charitable contribution (as defined in subsection (c)) payment of which is made within the

taxable year. A charitable contribution shall be allowable as a deduction only if verified under regulations prescribed by the Secretary or his delegate.

* * *

(26 U.S.C. 1964 ed., Sec. 170.)

SEC. 172. NET OPERATING LOSS DEDUCTION.

(a) Deduction Allowed.--There shall be allowed as a deduction for the taxable year an amount equal to the aggregate of (1) the net operating loss carryovers to such year, plus (2) the net operating loss carrybacks to such year. For purposes of this subtitle, the term "net operating loss deduction" means the deduction allowed by this subsection.

(b) [as amended by Sec. 317(b), Trade Expansion Act of 1962, P.L. 87-794, 76 Stat. 872] Net Operating Loss Carrybacks and Carryovers.--

* * *

(2) Amount of carrybacks and carryovers.--Except as provided in subsections (i) and (j), the entire amount of the net operating loss for any taxable year (hereinafter in this section referred to as the "loss year") shall be carried to the earliest of the taxable years to which (by reason of paragraph (1)) such loss may be carried. The portion of such loss which shall be carried to each of the other taxable years shall be the excess, if any, of the amount of such loss over the sum of the taxable income for each of the prior taxable years to which such loss may be carried. ***

* * *

(c) Net Operating Loss Defined.--For purposes of this section, the term "net operating loss" means (for any taxable year ending after December 31, 1953) the excess of the deductions allowed by this chapter over the gross income. ***

* * *

(26 U.S.C. 1964 ed., Sec. 172.)

Treasury Regulations on Income Tax (1954 Code):

§1.152-1 General definition of a dependent.

* * *

(2) (i) For purposes of determining whether or not an individual received, for a given calendar year, over half of his support from the taxpayer, there shall be taken into account the amount of support received from the taxpayer as compared to the entire amount of support which the individual received from all sources, including support which the individual himself supplies. ***

* * *

(26 C.F.R., Sec. 1.152-1.)

§ 1.170-1 [as amended by T.D. 6785, 1965-1 Cum. Bull. 117] Charitable, etc., contributions and gifts; allowance of deduction.

(a) In general.--***

(2) Information required in support of deductions for taxable years beginning before January 1, 1964. In connection with claims for deductions for charitable contributions paid in taxable years beginning before January 1, 1964, taxpayers shall state in their income tax returns the name and address of each organization to which a contribution was made and the amount and approximate date of the actual payment of each contribution. Any deduction for charitable contribution must be substantiated, when required by the district director, by a statement from the organization to which the contribution was made indicating whether the organization is a domestic organization, the name and address of the contributor, the amount of the contribution, and the date of its actual payment, and by such other information as the district director may deem necessary.

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(26 C.F.R., Sec. 1.170-1.)